Defective Pricing Basics

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SMC Points of Contacts Defective Pricing Issues

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DCAA Post-Award Audit Five Points to Establish Defective Pricing

When a contract price was negotiated and:

- The information in question fits the **definition** of cost or pricing data.
- Accurate, complete, and current data **existed** and were **reasonably available** to the contractor **BEFORE** the date of agreement on price.
- Accurate, complete, and current data were **not submitted or disclosed** and the government (CO or representative) did **not** have actual knowledge of this data or its significance to the proposal.
- The government **relied** on the defective data in negotiating with the contractor.
- The government's **reliance** on the defective data caused an **increase** in the contract price.

What we <u>will</u> cover today:

- **Truth in Negotiations Act and FAR**
- **Definition of Cost or Pricing Data**
- **Facts versus Judgment**
- **Defective Cost or Pricing Data Prior to Date of Negotiation**
- **PNM File Documentation**
- **TINA Remedy for Defective Pricing**
- **DCAA Audit Program for Defective Pricing Audits**

What we will not cover today:

- **Subcontract Defective Pricing**
- **Offsets**
- **Contractor “Sweeps”**
- **Penalties and interest**
- **Other**

Truth in Negotiations Act (TINA)

- The **purpose** of the TINA is to put the government on **equal footing** with contractors when negotiating contracts requiring cost or pricing data.
- TINA **requires** contractors to submit accurate, complete, and current cost or pricing data when negotiating contracts with the government.
- TINA provides the government with a **price reduction remedy** if a contractor fails to comply. The price reduction remedy takes effect when the contractor **does not** submit accurate, complete, and current data for a contract and the government **relied** on that defective data in determining the contract price.
- TINA requires contractors to submit and **certify** that their cost or pricing data is accurate, complete, and current.

Truth In Negotiations Act

Public Law:

- For **DoD**, NASA, and the U.S. Coast Guard
  - Section 2306(a) of Title 10, of the United States Code.
- For **other executive agencies**
  - 41 U.S.C. 254(b)

Regulation:

- **FAR Parts 15 and 52** implement the TINA.

Applicability of TINA

- TINA applies to negotiated prime contracts, subcontracts, and modifications where the government **required** cost or pricing data.
- TINA **extends** to interdivisional work, final price re-determinations, equitable adjustments, and termination settlements.
- TINA applies to **modifications** of **competitively awarded contracts** when the modification **exceeds** the applicable dollar threshold.
- TINA also applies to **change orders** when the **absolute value** of the increase and decrease exceeds the applicable dollar thresholds, even though the net change in price itself is under the threshold.

Dollar Threshold

- **Current TINA Dollar Threshold for DoD prime contracts and any subcontracts and modifications awarded under those prime contracts is:**

- **$550,000**

Cost or Pricing Data Defined
(FAR 2.101)

- Means all **facts** that, as of the **date of price agreement** or, if applicable, an earlier date agreed upon between the parties that is as close as practicable to the date of agreement on price, **prudent** buyers and sellers would **reasonably expect to affect price negotiations significantly.**
- Are **factual**, **not judgmental**, and are **verifiable**.
- **Do not** indicate the accuracy of the prospective contractor's **judgment** about **estimated** future costs or projections, but they **do** include the **data forming the basis for that judgment**.
- Include **more** than **historical accounting data**. They are **all the facts** that can be reasonably expected to contribute to the soundness of estimates of future costs and to the validity of determinations of costs already incurred.

Cost or Pricing Data Defined
(FAR 2.101)

- Include such factors as:
  - Vendor quotations
  - Nonrecurring costs
  - Information on changes in production methods and in production or purchasing volume
  - Data supporting projections of business prospects and objectives and related operations costs
  - Unit-cost trends such as those associated with labor efficiency
  - Make-or-buy decisions
  - Estimated resources to attain business goals
  - Information on management decisions that could have a significant bearing on costs.

Facts Versus Judgments

- **Judgments** are **not** cost or pricing data and **do not** become cost or pricing data when intertwined with facts.
- However, the **facts** underlying the judgments are cost or pricing data.
- When data contains judgments and facts that are so **intertwined** they cannot practically be segregated, **the entire data is subject to disclosure.**
- However, **only the facts require certification**.
- This means documentation should be **disclosed as cost or pricing data** if it meets all the definitional requirements of the FAR and contains elements of **both fact and judgment and the factual content has not otherwise been disclosed** in a meaningful manner.

Facts vs. Judgment

Example:

- A purchase order or vendor quote is usually considered cost or pricing data.
- Escalation applied to the purchase order or vendor quote is most likely an estimate.
- However, the contractor may have based the escalation on prior purchases or usage. Any judgments the contractor applies to such prior purchases or usage to estimate escalation are not cost or pricing data, but the actual purchases or usage are.

Facts vs. Judgment

Example:

- Contractor management discussions about whether or not to modernize a production line would not be cost or pricing data. It is a fact that discussions have been held, but a decision to act has not yet happened.
- On the other hand, a decision to modernize, even though the particular method of modernization has not been established, is cost or pricing data which must be disclosed.

Instructions for Submission of Cost or Pricing Data

The contracting officer shall specify in the solicitation:

- Whether cost or pricing data are required.
- The format for submission of cost or pricing data
  - Table 15-2 of FAR 15.408,
  - specify an alternative format, or
  - permit submission in the contractor's format.

FAR 15.403-4
Requiring Cost or Pricing Data

Where no exceptions apply, the contracting officer must obtain cost or pricing data before accomplishing any of the following actions expected to exceed the current threshold ($550,000) or, in the case of existing contracts, the threshold specified in the contract:

- The award of any negotiated contract.
- The award of a subcontract at any tier, if the contractor and each higher-tier subcontractor were required to furnish cost or pricing data.

FAR 15.403-4 Requiring Cost or Pricing Data (cont)

- The modification of any competitively awarded or negotiated contract or subcontract in excess of the threshold.
  - Price adjustment amounts must consider both increases and decreases (*e.g.*, a $200,000 modification resulting from a reduction of $400,000 and an increase of $200,000 is a pricing adjustment exceeding $550,000).
- Negotiated final pricing actions (i.e. terminations and final price agreements for fixed-price incentive and re-determinable contracts) where:
  - (A) The total final price agreement for such settlements or agreements exceeds the threshold ($550,000) or
  - (B) The partial termination settlement plus the estimate to complete the continued portion of the contract exceeds the threshold.

Requirement for Submission

When cost or pricing data are required, the contracting officer shall require the contractor to submit the following in support of any proposal:

- The cost or pricing data.
- A certificate of current cost or pricing data, in the format specified in 15.406-2, certifying that to the best of its knowledge and belief, the cost or pricing data were accurate, complete, and current as of the date of agreement on price or, if applicable, an earlier date agreed upon between the parties that is as close as practicable to the date of agreement on price.

Certificate of Current Cost or Pricing Data

"This is to certify that, to the best of my knowledge and belief, the cost or pricing data (as defined in section 2.101 of the Federal Acquisition Regulation (FAR) and required under FAR subsection 15.403-4) submitted, either actually or by specific identification in writing, to the contracting Officer or to the Contracting Officer's representative in support of ____* are accurate, complete, and current as of ____**. This certification includes the cost or pricing data supporting any advance agreements and forward pricing rate agreements between the offeror and the Government that are part of the proposal."

Contracting Officer's Designated Representatives for Receiving Cost or Pricing Data

The Board of Contract Appeals has held that submission of cost or pricing data by a contractor to a **field pricing support** activity can constitute **adequate** submission under TINA.

- Field pricing activity can include the **buying command staff** (buyer, contract specialist, technical), the **contract administration staff** (DCMA) responsible for activity at the contractor's location (pricing, contract administration, technical), and **DCAA**.

Reasonably Available

- Cost or Pricing data within the contractor's organization on matters significant to contractor management and to the Government **will be treated as reasonably available.** What is significant depends upon the circumstances of each acquisition.
- If the contractor had information **reasonably available** at the time of agreement showing that the negotiated price was **not** based on accurate, complete, and current data, **the contractor's responsibility is not limited by any lack of personal knowledge** of the information on the part of its **negotiators**.

Defective Data Prior to Date of Agreement on Price

- If, **before agreement on price**, the contracting officer (or representative) **learns** that any cost or pricing data submitted are **inaccurate, incomplete, or noncurrent**, the contracting officer shall **bring the matter to the attention of the prospective contractor**, whether the defective data **increase or decrease** the contract price.

- The contracting officer shall consider **any new data submitted** to correct the deficiency, **or consider the inaccuracy, incompleteness, or noncurrency of the data when negotiating the contract price**.

- The **price negotiation memorandum** shall reflect the adjustments made to the data or the corrected data used to negotiate the contract price.

[FAR 15.407-1(a)]

Documenting the Negotiation

In the Price Negotiation Memorandum, the contracting officer shall document the extent to which he or she --

- **Relied** on the cost or pricing data submitted and used in negotiating the contract price
- Recognized as inaccurate, incomplete, or noncurrent any cost or pricing data submitted, including
  - the action taken by the contracting officer and the contractor as a result, and
  - the effect of the defective data on the price negotiated.

Defective Cost or Pricing Data

If, after award, cost or pricing data are found to be **inaccurate, incomplete, or noncurrent** as of the date of final agreement on price, the Government is entitled to a **price adjustment, including profit or fee**, of **any significant amount** by which the price was increased because of the defective data.

- **FAR 52.215-10**, Price Reduction for Defective Cost or Pricing Data, and
- **FAR 52.215-11**, Price Reduction for Defective Cost or Pricing Data -- Modifications.

Defective Cost or Pricing Data

These contract clauses recognize that the Government's right to a price adjustment is **not** affected by any of the following circumstances:

- The contractor or subcontractor was a **sole source supplier** or otherwise was in a superior bargaining position
- The contracting officer **should have known that the cost or pricing data at issue were defective** even though the contractor or subcontractor took no affirmative action to bring the character of the data to the attention of the contracting officer
- The contract was based on an **agreement about the total cost** of the contract and there was no agreement about the cost of each item procured under such contract, or
- The **contractor or subcontractor failed to submit** a Certificate of Current Cost or Pricing Data relating to the contract.

Suspected Defective Pricing

- If, after award, the contracting officer **learns or suspects** that the data furnished **were not**
  - accurate, complete, and current, or
  - adequately verified by the contractor as of the time of negotiation,

  the contracting officer shall **request an audit** to evaluate the accuracy, completeness, and currency of the data.

[FAR 15.407-1(c)]

DCAA Post-Award Audit Five Points to Establish Defective Pricing

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DCAA Audit - Contract Selection Process

Contract Selection –

- Risk Determination Level Drives the number of Contracts Selected for Audit
- Contract Selection Criteria Includes Contract Type and Dollar Value and is Weighted toward FFP and FPI
- CPFF and CPAF contracts will be selected for audit only where audit leads exist (includes PCO requests) or where there is an overall likelihood of defective pricing:
  - High Risk Contractors – Contract Value >$100M

Initial Audit Procedures

- Coordinate with the PCO:
  - At the **start** of the audit
  - **During** the Audit
  - At the **conclusion** of the Audit
- Obtain Price Negotiation Memorandum (PNM)
  - Determine what Cost or Pricing Data were **Provided and When**
  - Whether the PCO **Relied** on such Data
  - Any **Considerations** made by the Contracting Officer during negotiations that impacted cost or pricing data
  - **Other** Factual Considerations that Influenced the negotiations
- At the start of the Audit **confirm** with the PCO that the Gov't r**elied** on the cost or pricing data

Possible Indicators

Examples:

- Significantly lower actual cost of individual items and cost elements as compared to the amounts in the audit baseline.
- Operations not actually performed or items of cost not incurred, although included in the contractor's proposal.
- After submitting the original proposal but before price agreement, the contractor receives a firm quote from an established source which is significantly below the cost included in the original proposal.

Possible Indicators

Examples:

- Less obvious indicators may include the contractor's failure to reflect in the proposal decisions expected to lower costs. This usually relates to budgets, production, automation, and make or buy decisions when the management decision has been made and the information was available, but not disclosed, before agreement on price.

Determining Potential Defective Data

- **Compare** the cost or pricing data in the audit baseline to all accurate, complete, and current data **reasonably available** to the contractor prior to the date of agreement on price…
- Differences found **identify potential** defective pricing.
- For each difference, **establish the five points** needed to prove defective pricing.

Coordinate Potential DP Finding with PCO

When apparent DP is found, and the materiality threshold is met ($50,000), the auditor will discuss the findings with the PCO:

- Request the PCO confirm in writing –
- The apparent defective cost or pricing data was **not disclosed** to PCO or representative
- That **neither** the PCO or representative had actual **knowledge** of the data, and
- That the PCO **relied** on the defective data in negotiating a price.

Coordinate Draft Audit Rpt with PCO

- At the conclusion of the audit, provide to the PCO with
  - The draft report exhibits and notes explaining the audit position, and
  - Copies of disputed documents and other significant audit evidence.
- Obtain PCO comments on the factual matter involved.

Obtain Contractor Comments

- Provide to the contractor for comments --
  - The draft report exhibits and notes explaining the audit position, and
  - Copies of disputed documents and other significant audit evidence.
- Include any contractor comments received in the audit report to minimize delays in resolution.

DCAA Audit Report

- An audit report is required for all defective pricing audits.
- Each audit report with a recommended price adjustment must --
- specifically list the five points for defective pricing in the notes to the report exhibit, and
- Discuss how each point has been met.
- Address the audit report to the PCO

Questions

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